ACCOUNTANCY

Published by
The Society of Incorporated Accountants and Auditors
Incorporated Accountants' Hall
Victoria Embankment
London, W.C.2

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VOL. LV (Vol. 6 New Series) **December, 1943** **Number 604**

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PROFESSIONAL NOTES

Costing and Price Fixing

The fourteenth report of the Select Committee on National Expenditure is devoted to a searching review of the methods employed in fixing prices under war contracts, and is therefore of exceptional interest to accountants. Recognising that the most important consideration in settling prices is that these should stimulate efficiency and economy in production, the Committee have kept incentive factors well to the fore in examining the methods of cost investigation and price fixing employed by the various Departments. The method most likely to give the necessary stimulus, it is pointed out, is to give the contractor a fixed price. This is, for example, the most effective means of ensuring that main contractors carry out their responsibility of checking sub-contractors' prices. To make exact cost ascertainment a general practice leads in any case (as the experience of the Ministry of Supply has shown) to an entirely unmanageable volume of work, apart from the overriding consideration that "a method of payment according to what a contractor can show he has spent is intrinsically a bad method." It is agreed that the investigating accountants of the Ministry of Supply are now given full instructions for the determination of overheads. On the other hand, the Committee finds that the method of post-costing is still employed to an unnecessary extent. Figures are quoted to justify the conclusion that "experience ought by now to have shown the Ministry fairly clearly that there are certain firms with which they can safely negotiate fixed prices, and thus supersede the cumbrous method of maximum prices subject to post-costing, while there are others which require special treatment." Though considerable progress is shown in the trend towards a fixed price basis, however, the Committee hold that "this policy has not in practice been operated so as to realise its full advantages." Either the policy has not been applied widely enough or the actual fixing of prices has been deferred to an unduly late stage in the execution of contracts.

Real Costs versus Overheads

On the subject of costing, many of the Committee's criticisms and recommendations will be familiar to readers of ACCOUNTANCY. Given the safeguard of E.P.T., the Committee points out, "looseness about costs must be much more damaging than looseness about profit margins." From this point of view, the conclusion is inevitable that much of the time and energy absorbed in cost investigations has not been used to the best advantage: "There has been a tendency to concentrate attention on profit margins and on the allocation of overhead charges to a degree which has been disproportionate to the attention given to the much more important question of economy in real costs." Another familiar criticism is of the striking lack of uniformity in the

methods of the three main supply Departments, which does not seem to the Committee to be fully justified by differences in the nature of the main stores for which each is responsible. "The existing machinery has not succeeded in producing adequate co-ordination and uniformity." In particular, "if the interpretation of the responsibility of a Director of Production is limited to getting output, and of a Director of Contracts to seeing that manufacturers do not get paid more than their costs justify, there will be neglect of the vitally important responsibility for seeing that the required output is obtained with maximum efficiency and minimum absorption of national resources." It is in more effective attention to this responsibility that the Committee see the chief scope for improvement in existing practice. In general, the impression is that the Committee's criticisms are balanced and the recommendations are not, as might so easily be the case, mere counsels of perfection. It is hoped to deal with the Report more fully in a future issue.

Mr. C. J. G. Palmour

At a meeting of the Council of the Institute of Chartered Accountants on November 3, Mr. C. J. G. Palmour, President of the Institute, was presented with his portrait painted by Mr. Frank Salisbury, C.V.O., R.P., R.O.I., R.I. A replica was presented to Mrs. Palmour. The Vice-President, Mr. H. M. Barton, presided. Lord Plender, the senior member of the Council, in making the presentation, said it was fitting that in Mr. Palmour's sixth year of office his colleagues on the Council and the Past Presidents should wish to mark their admiration of him in a way that would preserve his name and appearance to future generations of Chartered Accountants. Mr. Palmour had ever been mindful of the highest traditions of the profession, and he was respected for his sound judgment, impartiality, and fair-mindedness. When the record of his Presidency was written, his name would be among the outstanding figures who had held that high office. They wished health and strength for many years to both Mr. and Mrs. Palmour. Mr. Palmour, in reply, expressed his pride that his portrait would hang in the Hall of the Institute with that of his former senior partner, Mr. Frederick Whinney. The painting had led to a new and most pleasant friendship with the artist, Mr. Frank Salisbury. Mrs. Palmour also expressed her thanks in a short speech.

The Profession and Public Life

The Minister of Labour and National Service and the Minister of War Transport have jointly appointed a committee on seamen's welfare in ports. The chairman is Mr. H. Graham White, M.P., and among the members of the committee is Mr. Richard A. Witty, President of the Society of Incorporated Accountants.

Mr. T. Harold Platts, F.S.A.A., a member of the Council of the Society of Incorporated Accountants, has been elected Mayor of Droitwich.

The following were among those nominated by the Right Hon. the Lord Chancellor as Sheriffs for Counties in England and Wales at the annual ceremony on November 12:—

Mr. Joseph Stephenson, O.B.E., F.S.A.A.: Cambridgeshire and Huntingdonshire.

Mr. R. Wilson Bartlett, J.P., F.S.A.A.: Monmouthshire.

Mr. R. Wynne Bankes, C.B.E.: Flintshire.

Mr. Roland C. Larking, F.C.A., F.S.A.A., has been appointed High Sheriff for the City of Norwich.

Mr. L. T. Little, B.Sc., the Deputy Secretary of the Society of Incorporated Accountants, who is temporarily in Government service, has been promoted and has been appointed an Assistant Secretary (temporary) of the Ministry of Aircraft Production.

Company Law Amendment Committee

The Departmental Committee of the Board of Trade, under the chairmanship of Mr. Justice Cohen, which is considering what major amendments are desirable in the Companies Act, 1929, has already held several meetings, and the first three days' minutes of evidence have now been published by H.M. Stationery Office. The Committee heard oral evidence and considered memoranda submitted by Mr. Percy Martin and Mr. P. J. Rose, C.B., Registrars of Companies for England and Scotland respectively, on September 17; by Mr. H. P. Naunton, D.S.O., Official Receiver in Companies Liquidation, and Mr. L. A. West, Senior Official Receiver in Bankruptcy, on September 24; and by Sir John Fox, O.B.E., Chief Registrar of Friendly Societies, on October 1. A summary of the principal suggestions put forward by these witnesses is given on page 49 of this issue. The publication of further evidence will be awaited with interest, and we propose, if space permits, to keep our readers informed month by month, of the views expressed before the Committee.

'Salute the Soldier'

Following the Warships Weeks of 1941 and the Wings for Victory campaign of 1942, it will be the turn of the land forces to provide the focus of enthusiasm for next year's special savings drive. This will take the form, as was announced at the Mansion House recently, of a series of "Salute the Soldier" weeks, beginning with a London week opening on March 25, and extending into July. In the fourth year of the war savings campaign, which ended in the latter half of November, small savings are estimated to have produced £741 million, and large savings £1,187 million. Though the total of £1,928 million thus includes 38 per cent. of small savings, and also shows an increase on the year of £210 million, Lord Kindersley has called attention in a broadcast to the disappointing trend of small savings in recent months. After averaging £15,500,000 a week in the first two months of the year, and as much as £18,000,000 a week during the Wings for Victory campaign, subscriptions later fell away to a weekly average of only £11,500,000. Since the holiday season is long past, the only conclusion seems to be that the series of war successes has led to a relaxation instead of a stimulation of efforts on the savings front. Before

the spring, however, it may be that great events nearer home will have led to a renewal of enthusiasm that will make the special campaign of next spring an even greater success than its predecessors.

Research in the Transvaal

A Research Committee is being formed under the ægis of the University of the Witwatersrand, the Transvaal Society of Accountants, and the South African (Northern) Branch of the Society of Incorporated Accountants. Preliminary discussions took place between Mr. G. H. R. Edmunds, F.S.A.A., President of the Transvaal Society, and Professor Richards, of the Witwatersrand University. Each of the three bodies is to appoint two members of the Committee, which will have power to co-opt additional members to assist in specific research work. The two Incorporated Accountants appointed to represent the South African (Northern) Branch are Mr. R. B. Sinclair and Mr. K. L. Smith. The new Research Committee will have the good wishes of all Incorporated Accountants, and particularly of all who are concerned in the work of the Incorporated Accountant's Research Committee which is functioning in Great Britain.

War Damaged and Destroyed Houses

An article in our last issue dealt with "Sales of War Damaged Properties," and gave some guidance to owners of property and their advisers on the principles determining whether a cost of works payment or a value payment should be expected. Because the provision of housing accommodation is in the public interest, the Treasury has issued a new direction to the War Damage Commission. In the case of houses built after March 31, 1914, or houses built earlier if before the war damage the structure was unimpaired and the design, lay-out and amenities were reasonably equal to those of newer houses, the Commission may now make a cost of works payment, covering the reasonable cost of restoration or rebuilding, even where the house is totally destroyed. In addition, the Commission may pay the reasonable cost of repairs to houses where there is no structural damage or where repair would have been reasonable if the condition had been caused by non-war causes. "House" includes flats, tenements, and any properties comprising living accommodation where only the ground floor and basement are used for business or other purposes. The new powers are not to be operated where injustice would be caused to any person interested in the kind of payment to be made. A cost of works payment is only made after the work has actually been carried out. Execution of the work remains subject to any necessary planning or other consents; and, where the cost together with the cost of other work on the property during the preceding twelve months exceeds £100, a building licence must be obtained from the Ministry of Works. Most of the owners of seriously-damaged property, the classification of which may be affected by the legislation of 1943 or by the new direction, will shortly receive a notification stating whether, in the opinion of the War Damage Commission, the property is a "total loss" or not.

Meetings in London

"Government Price Control" will be the subject of informal discussion at a meeting of the Incorporated Accountants' London and District Society on Wednesday, December 1, at 4 p.m. The discussion will be opened by Mr. C. V. Best, F.S.A.A., and the chair will be occupied by Mr. F. Martin Jenkins, F.S.A.A., Vice-Chairman of the District Society. It is hoped to arrange further meetings for the discussion of current professional topics. Members who are interested are asked to notify the Secretary immediately, if they have not already done so, in order that notices may be sent to them. Members of the District Society are also cordially invited to the meetings of the Incorporated Accountants' Students' Society of London and District. A helpful series of three lectures on taxation matters will be concluded on December 9 at 4-30 p.m. when Mr. Joseph Stephenson, O.B.E., F.S.A.A., will deal with "Taxation of Farming Profits." The Students' Society hopes in due course to publish the text of this lecture and of the discussion which will follow, together with those previously given by Mr. H. A. R. J. Wilson, F.C.A., F.S.A.A., on "Deduction of Tax from Salaries and Wages," and by Mr. H. Heathcote-Williams, M.A., Barrister-at-Law, on "E.P.T. Problems."

Employers and "Pay As You Go"

The passing of the Income Tax (Employments) Act leaves to be solved later a number of problems connected with the scope of the tax and the transitional arrangements necessary for bringing it into force. Even more urgent, perhaps, are the technical difficulties of administering the system as it stands. It is believed that the unduly heavy "swing" in tax deductions has now been largely overcome. No official steps, however, appear to have been taken with a view to reducing the burden which will fall on employers on the rush of pay day. This is a serious matter; in present conditions of staff shortage many employers fear the system may be practically unworkable. It remains to be seen what can be done at this stage, but it is fairly clear what sort of solution should be aimed at. It should retain the useful *principle* of cumulative taxation, which is best able to minimise the danger of over-deduction, while avoiding the use of the cumbrous cumulative tax *tables* during the hurry of pay day. Several schemes have been evolved along these lines. The usual principle is to base weekly deductions on some simple weekly tax tables, and to use the Inland Revenue's cumulative tables for periodical balancing operations. The weekly tables may be cumulative in character, in that they determine whether tax should be deducted at the reduced or full rates, having regard to aggregate earnings to date, and assuming that they will continue at this level for the whole year; or they may be entirely non-cumulative and merely set the appropriate portion of the tax-payer's annual allowances against his earnings in any given week. A scheme of the latter type has been prepared by Mr. J. Clayton, A.C.A., and is apparently being considered as an optional method for individual industries. An article on the Act is on page 52.

ACCOUNTANCY

Formerly the Incorporated Accountants' Journal
Established 1899

The Annual Subscription to ACCOUNTANCY *is 12s. 6d., which includes postage to all parts of the world. The price of a single copy is 1s. 0d., postage extra. All communications to be addressed to the Editor, Incorporated Accountants' Hall, Victoria Embankment, London, W.C.2*

PROVISIONS AND RESERVES

In this strenuous period the time of professional men is very fully occupied, and professional organisations are attempting with inadequate staffs to maintain their normal routine and to cope with additional heavy tasks. It is therefore commendable that the Institute of Chartered Accountants should have embarked on an educational programme, of which the sixth section was published in October. This is another of the many examples of the effect of war in stimulating a greater intensity of thought and a more acute awareness of the shortcomings of existing forms and of the possibilities of development and improvement. We welcome this sign that the accountancy profession is alive to the spirit and challenge of the times.

Any attempt to define accounting principles is open to the twin dangers which beset all who set out to enunciate principles—that of being vague and inconclusive, and of being trite and obvious. The latest pronouncement on reserves and provisions avoids neither of these dangers completely. It is vague and inconclusive in that throughout it makes no direct reference to the profit and loss account and offers no guidance as to the entries in that account by which effect can best be given to the recommendations made. And it is trite and obvious in that it repeats what has been said frequently by the more advanced thinkers in the profession since the whole subject of reserves was forced on the notice of the public, as well as of the profession, by the *Royal Mail* case over ten years ago. But if the pronouncement is less specific and definite than could be desired, it is none the less to be welcomed, because it will strengthen the hands of those who are working for more informative accounts. It must be noted, moreover, that the recommendations are of an interim character and may be leading up to a detailed consideration of the contents of the profit and loss account.

It may be open to argument whether uniformity in accounts is desirable, even if it were possible; but there can hardly be any difference of opinion as to the desirability of standardising nomenclature, and the recommendations defining and limiting the use of the words "Provisions" and "Reserves" are the most valuable part of the latest pronouncement. It is appropriate to point out that the distinction drawn was explicitly expressed in the report to the Council of the Society, drawn up by a sub-committee appointed to consider what alterations in law and in practice were considered to be necessary as a result of the disclosures in the *Royal Mail* case. The report was made in April, 1932, and we make no apology for quoting Clause C of its recommendations:—

> "That Free Reserves should be disclosed on the face of the balance sheet. The need for such disclosures should not extend to provisions made for estimated losses or expenses not definitely ascertainable at the date of making up the company's accounts, but to which losses or expenses it is sound and proper to have regard in arriving at the profit or loss for the year or other period."

That report anticipated the latest pronouncement of the Institute, but it went more deeply into the real problem underlying the setting out of reserves in a balance sheet. That problem is how best to disclose the creation and utilisation of provisions and reserves so that the accounts shall convey an accurate and, as far as may be, a complete picture of the state of the company's affairs. The Society's Committee observed a proper priority when it recommended that "The profit and loss account should show the true balance of profit or loss for the period covered by such account," and further that "in the profit and loss account any debits or credits which are abnormal in character or extraneous in their nature to the ordinary transactions of the company, together with any reserves from a previous period no longer required, should be stated separately." The implications of these recommendations were very far reaching, and we draw the attention of our readers to them because they seem to us to supplement and complete the recommendations which have now come from the Council of the Institute. For the abuse which the recommendations are designed to prevent is that of the improper manipulation of reserves so as to inflate or deflate profits without disclosure to those who are entitled to the information, and this can only be effectively prevented if the profit and loss account as well as the balance sheet conforms to the principles laid down.

The Institute's recommendations are set out in full on page 51 and the authors may reasonably claim that their main purpose is the clarification of the information disclosed in published accounts and the extension of the number of companies whose accounts reflect the influence of the best professional practice rather than the checking of abuse. That purpose has our entire support; and, limited though such an aim may be, the application (for example) of the recommendation that fixed assets should be shown at cost and provisions for depreciation and diminution in values should appear as separate deductions therefrom might well produce interesting and even startling revelations in some cases. Unexpected results do sometimes emerge from the following of principles, but accounting principles are likely to be most fruitful when they permeate rather than explode.

Income Tax "Concessions" and "Arrangements"

By W. B. COWCHER, O.B.E., B.Litt., Barrister-at-Law

In an article in the October issue of this journal on the valuation of trade debts for income tax purposes, it was pointed out that the Court of Appeal judgments in *Absalom* v. *Talbot* (C.A., April 20, 1943, T.R. 119), also raised the general question of the validity of Revenue " concessions." But whilst du Parcq, L.J., in his judgment had declared that Parliament alone could mitigate the harshness of income tax law in relation to the valuation of trade debts, Scott, L.J., had spoken even more emphatically upon the subject. " Is the practice (*a*) legal, (*b*) devoid of legal sanction, or (*c*) contrary to law and therefore prohibited ? " But, not content to confine his comments to the question immediately before him, he extended his remarks to Revenue " concessions " generally :—

> " No judicial countenance can or ought to be given in matters of taxation to any system of extra-legal concessions. Amongst other reasons, it exposes Revenue officials to temptation, which is wrong, even in the case of a service like the Inland Revenue, characterised by a wonderfully high sense of honour."

The subject is one of importance and involves difficult problems, particularly in regard to administration. Its origin lies in the complexity of modern finance and industry with their ever-changing economics. Thus, as has been seen, the law as to trade debts laid down by the Privy Council in *Gleaner Co.* v. *Assessment Committee* (1922, A.C. 169), whatever it may be in regard to ordinary trade debts, is obviously inequitable and unsuitable in connection with hire-purchase contracts, and any such flaw in the legal machinery will increase in importance as the pressure of taxation becomes heavier. Legislation to remove anomalies is usually a much slower process than that to stop leaks and evasions ; and, in the meantime, maladjustments working against the taxpayer are often dealt with by " concessions " or " arrangements " which have no legal sanction. These are of several kinds ; four classes, at least, are to be found :—

1. Where the law as previously interpreted is altered and made harsher and more inequitable by legal decision but the decision is not allowed to alter previous practice. The *Gleaner* judgment is in point, but there have been other cases.
2. Where the strict law is administratively difficult and would entail trouble to both the Revenue and the taxpayer. The Building Societies' " Arrangement " is an attempt to solve the tax problem of monthly payments consisting of capital and interest.
3. Where a relief manifestly due in equity is not obtainable under the existing law. The relief in respect of bank interest paid now given by Section 36 of the Income Tax Act, 1918, was first made law by the Finance Act, 1915, but had been a " concession " for many years previously. So also had the allowance for obsolescence of plant and machinery, now Rule 7 of Cases I and II of Schedule D.
4. Where more than one interpretation of, or method of carrying out, a statutory provision is possible, and the one chosen by the Revenue is normally most favourable to the taxpayer.

Altogether, the number and importance of " concessions " and concessional " interpretations " is very large and, difficult as the problem is, the necessity of dealing with it is indicated by the significant fact that early knowledge of a new example has a certain market value.

Reverting to the question of legality, it is somewhat remarkable that in the *Absalom* case the liking by Scott, L.J., for historical research did not lead him to a consideration of the constitutional conflict between Parliament and the Crown which ended in 1688 with the Bill of Rights. Although taxation without the consent of Parliament may have been originally the great issue, in the time of James II, it was the Crown's claims to be able to grant dispensations from and to suspend the operation of laws which were the chief bones of contention. Revenue " concessions " which, and to the extent that they do, result in official practice not in conformity with the tax laws imposed by Parliament are clearly unconstitutional ; and the objections to be urged against them are those which inevitably arise. In the first place, there is absence of publicity, although this is mainly remediable. It is very necessary, assuming a Revenue right to make " concessions," that in the interests of justice and equality between taxpayer and taxpayer their existence and nature should be matters of public knowledge.

The next objection is equally serious. So long as anything is claimed to be a "concession "—some so-called " concessions " are as stated not concessions but alternative interpretations—the taxpayer has no rights ; and the Department can dictate not only what shall be the " geographical " limits of its application but also the extent and circumstances of the relief. No right of appeal can possibly arise in connection with a non-legal concession, and the Department is in the position of a despot. And despotism, however benevolent, is not appreciated in this country.

Nevertheless, the great complexity of modern finance and commerce makes it impossible to administer income or profits taxation without administrative rules and precedents, some of which will inevitably be open to criticism from the standpoint of constitutional law ; and the question arises whether the Revenue should not be enabled to make " concessions " and " arrangements " within strictly defined limits. As regards limitation, no power should be given to increase the statutory burden upon the taxpayer, except in so far as a relief given to one increases the burden upon the rest. Whilst, however, the power to make administrative rules in order to carry out in particular cases and circumstances the manifest

intentions of Parliament, and to deal with minor points of principle, might be given, it would seem to be vitally important to avoid the danger, always imminent, of taxation by Regulation superseding taxation by Act of Parliament. In the writer's opinion, whilst the subject is of sufficient importance to warrant an investigation by a Committee, there is a strong case for allowing the Revenue authorities who have acquired, and deservedly so, the trust and confidence of the public, the right to make concessions and arrangements in the interests of justice and public convenience.

One final remark. Every taxpayer should enjoy what in international trade is known as the "most-favoured nation" principle. There will always be the danger lest a "concession" may be granted under pressure to a powerful interest but may not be applied elsewhere although *on an appeal*, if necessary, it might be provable that there was an equal right based upon merits.

Current Aspects of Life Assurance

[CONTRIBUTED]

Life assurance is eminently suited to perform a double rôle for the man of small or medium means who derives his income from his own efforts. It is at once the simplest method of setting aside a provision which will enable him to retire from work at a reasonable age, and also the only means by which he can secure protection for his family from the consequences of his own untimely death. It has sometimes been suggested that increased State provision by means of comprehensive social services against all possible contingencies will lead to a contraction in the demand for life assurance. The needs which it meets are so universal, however, that it is much more likely that the guarantee by the State of a certain minimum standard will lead to a wider demand for additional provision over and above that standard, so as to accord more closely with the standard of life to which a large part of the people of this country are accustomed. Further, there has been a natural reluctance to commit too large a proportion of income to life assurance which, to an extent, is a "lock-up" investment. The assurance of a fair minimum income during periods of illness and unemployment should do much to remove this fear, and thus to enhance the popularity of life assurance.

The two aspects of a life policy—as an investment and as protection—have received varying emphasis at different periods. Up to the beginning of the present century the investment aspect was little to the fore, the majority of policies being taken for the whole of life. Endowment assurances were, however, already growing in popularity, and an immense impetus was given to them by the effects of the war of 1914-18. The investment opportunities then afforded to the companies (during a period of rapidly expanding funds), coupled with the substantial rebate from premiums resulting from the income tax allowance, enabled them to offer contracts showing yields purely as investments which could not even be approached by any other investment offering comparable security. Indeed, it could almost be said that the life assurance cover was thrown in as a make-weight! This period of high profits was brought to an end by the drop in interest rates at the time of the War Loan conversion of 1931, and far greater emphasis is now placed on the advantages of these contracts as a protection against the consequences of early death.

Interest Rates and Valuations

It is, of course, well known that anticipated interest earnings are incorporated as one of the factors in calculating the premiums to be charged. Thus a decline in interest rates not only affects the return which may be expected on new contracts, but leads to a number of difficult problems as regards policies already issued. Before considering these, it will be helpful to examine the methods by which the profits of life companies are estimated.

To those familiar only with the accounts of ordinary commercial companies, those of life assurance companies are apt to be confusing. It must, however, be borne in mind that the revenue account and balance sheet which they publish each year give no indication at all of the profits earned. They are, in fact, merely a record of the cash received by the company during the year, of the way in which it has been dealt with, and of the investments which represent the balance in hand at the end of the year available to meet liabilities. After deducting fixed liabilities, such as creditors, capital, etc., there remains a balance called the "Life Assurance Fund," which represents the ultimate amount available to meet the demands of policy-holders, if capital and reserves are to remain intact. It remains to compare this fund with the estimated liability to policy-holders, and this comparison is made in a separate "Valuation Balance Sheet" appearing in the 4th Schedule of the returns made to the Board of Trade, which need only be published every fifth year, although a number of companies do so every year.

In estimating this liability to policy-holders, the actuary must, of course, take account of the whole future period until all existing policies have gone off the books—which may be as long as 80 years, although some 30 years will usually account for the greater proportion of them. The principal factors entering into this estimate are interest, mortality and expenses. It will be readily understood that a heavy reduction in the rate of interest that can be earned will not only reduce current income, but will demand very careful consideration of the rate assumed for the future; if this latter has to be altered it will result in a very substantial increase in liability, which may absorb the whole of the current profits for a number of years.

Fortunately, life companies have for many years adopted a very conservative outlook. They have usually valued their liabilities at rates of 3 per cent. or less, even when earning much higher rates, and they are, therefore, in a strong position to meet the strain of current conditions. It must, however, be remembered that they are at present largely confined to Govern-

ment securities for their new investments and have to meet income tax which (even after a special concession as regards income reserved for policy-holders) remains at the high rate of 7s. 6d. in the £. In these circumstances, with-profit policy-holders cannot expect a return of the high bonus rates ruling before the present war, while the stiffening of non-profit rates which has already made considerable progress is likely to continue.

War Experience

The difficulties have, fortunately, not been aggravated by additional losses on the scale which was feared as a result of deaths caused by enemy action. Measured by the standard of 1914-18, these losses have, up to the present at any rate, been extremely light, and although under the majority of pre-war policies the companies have covered the full war risk, the resultant losses have not been too serious, and have been offset, at least partially, by a general improvement in mortality from other causes. Indeed, one company was able to announce that, even after including war claims, the mortality of its policy-holders in 1942 was less than anticipated by the table used in valuation, which was based on the experience of the years 1924-29. There is no reason to think that this result was exceptional, remarkable though it is in the third year of war, and a notable testimony to the achievements of the medical profession and the Ministry of Food.

At the outbreak of war the companies decided not to cover the war risk, whether in this country or abroad, for new policies except upon payment of a substantial additional premium. It is very gratifying that, as a result of experience, it has been found possible to relax these restrictions very substantially, at any rate so far as the risk in this country is concerned. During the past year, many companies have announced their readiness to issue policies giving cover against the war risk in this country upon payment of quite small extra premiums—usually 5s. per cent. or 10s. per cent.—or even, in a few cases, without charging any extra premium at all.

Industrial Assurance

It is usual to divide life business into two main sections. The first is the ordinary branch, with which the preceding paragraphs have been mainly concerned. The second is industrial business, which affects a numerically much larger part of the population, although owing to the small size of the policies issued, the total premium income involved is smaller. An interesting sidelight on the ubiquity of the operations of the industrial assurance companies was afforded by the tragic disaster at a London tube shelter in the early part of the year. It was announced that these companies paid out over £6,000 to the relatives and dependents of those who lost their lives on this occasion, and set up a special organisation to ensure that claims were speedily dealt with.

The most notable single event of the past twelve months, so far as this branch of the business is concerned, was the publication in November, 1942, of the Beveridge report. This contained drastic proposals for the nationalisation of industrial assurance, accompanied by severe criticisms of the conduct of the business. Thus was initiated a heated debate, which has continued sporadically ever since, in Parliament, press and elsewhere. Sir William Beveridge's main criticisms were on the score of expense and of the high lapse ratio. Perhaps the most apt comment on the former was made by Lieut.-Col. Sir Ian Fraser in Parliament. He said: "I pay £2 9s. a gallon for the petrol I put in my lighter, because I buy it in small quantities. It is really expensive, but that is the cost, with profits, of putting the petrol into little bottles and putting it into little retail shops. If you sell insurance by the penny, it is clearly very expensive, but that does not mean that it is bad." The companies maintain that, allowing for the service which they give, their expenses are very reasonable, and, apart from the unfortunate reference in the Beveridge report to the Hospital Contributory Associations and the War Savings Committee (both of which rely on voluntary efforts), there seems little attempt to dispute this, at any rate so far as the bulk of the business is concerned. The main point at issue is whether this home service is necessary, or whether the business could as well be run by a centralised system which would avoid frequent calls for the collection of small sums of money, but which, the companies maintain, would not meet either the wishes or the convenience of their policy-holders, to whom the insurance agent often acts as a kind of "poor man's lawyer."

The problem of lapses is one which has long had the serious attention of the companies themselves, for they have no desire to see policies which have been secured after considerable effort ended prematurely. It is often not realised outside insurance circles that nearly all offices grant automatic free policies, which represent a very reasonable return for the premiums paid, if premiums are discontinued after two or more years, while all offices are bound by statute to grant such free policies if premiums are discontinued when at least five years' payments have been made. Outright lapses, therefore, normally occur only in the case of very recently effected policies, and for two reasons frequently involve little or no loss to the policy-holder. In the first place, policies are not lapsed immediately they fall into arrear, with the result that, in the case of first year lapses for example, cover will be given on the average for nearly double the period for which premiums have been paid. Secondly, if a policy has fallen into arrear after a few weeks' payments, it is often to the policy-holder's advantage to lapse that contract and re-enter under a new one, which, if he has not passed another birthday, will be for the same amount as the original policy.

The Past Year

The past year may be summarised as a period which has brought many difficult problems and not a few worries to those responsible for the conduct of life assurance in this country. At the same time, there has been gratifying evidence of continued faith in the soundness and stability of the industry, for in spite of the extremely thorough comb-out of the outside staffs for transfer to national service, most companies were able to make new business announcements that would bear comparison with the high totals achieved just before the war..

The Measurement of Depreciation

By F. S. BRAY, Chartered and Incorporated Accountant

Among those expressions in accounting terminology which are difficult to define with any real precision, that of " depreciation " is well to the front. Nevertheless, it is a term applied to an important charge in the income statement of most undertakings, and is one which, apart from purely arithmetical calculations, gives accountants no little difficulty in measuring. It is well known that even like firms in the same industry may adopt different methods of providing for depreciation on their fixed assets, a situation which vitiates comparison between the net incomes of those firms.

We suggest that it is possible to distinguish three major elements in those happenings which, as related to assets, are covered by the accounting term—" depreciation." These elements may be conveniently expressed under the appellations of Value, Time and Use.

1. *Value.* This heading will take in all external changes in values involving losses which ultimately tend to settle down to that position where they come to be regarded as relatively permanent, and which thereby lend themselves to some stability of measurement in money terms. It is a conception which includes obsolescence.

2. *Time.* The emphasis on time is but a salutary reminder that all material things are transitory and, therefore, subject to some measure of disintegration. Dawson, in his *Accountants' Compendium* (London, 1930, p. 174), attempts a definition of depreciation which includes a shrinkage in the cost price or value of an asset due to the " mere effluxion of time." This comes near to the conception we are discussing, yet it is desirable to distinguish between the actual temporal deterioration of a physical asset and its related fall in value. We should also notice that temporal deterioration is ordinarily marked by the characteristic of gradualness. It is not a " jerky affair " due to some special cause, but a relatively smooth decline which is both natural and inherently inevitable : a character which should influence the basis of its measurement in money terms.

3. *Use.* This conception relates " depreciation " to " cost " in proportion as physical asset resources are used in production. A physical asset at any particular point of time is regarded as a store of future production units. The using up of such units is measured in terms of a direct cost of production. Thus depreciation is conceived as a productive " exhaustion of usefulness."

It may be objected that depreciation is subject to partial correction by current maintenance, an argument which the English double account system was thought to imply and which at one time brought that system under criticism. We suggest that, provided maintenance is distinguished from replacement, this objection rests upon a misconception, and that depreciation is a fact of experience which *follows after* an underlying basic assumption that every efficient enterprise will necessarily keep up a reasonable standard of maintenance.

At the present time there are a variety of methods of calculating depreciation, but there is one guiding canon which is fundamental to any attempt to establish uniformity of method. It is well expressed in the Report of the Committee of the American Institute on Terminology for 1942 on Depreciation, which states that " any method to be acceptable must provide for the distribution of the estimated total depreciation cost during the useful life of the property to which the amount relates, over accounting periods in a systematic and equitable manner." (Accounting Research Bulletin, No. 16 (Special), October 1942, p. 143.) This at once suggests a predilection for the " straight line " basis of calculating depreciation, which might well replace the somewhat artificial diminishing balance calculation which is so familiar a feature in many English accounts.

The practical problem concerning uniformity in the measurement of normal " depreciation," as specifically related to fixed assets acquired for operational purposes, mainly lies in the reconciliation of two methods of calculation, viz. :

1. The " straight line " method which, having regard to the guiding canon we have noticed, should have the pre-eminence, and

2. A basis of measurement related to output, preferably in terms of production centres (c.f. the familiar Machine Hour and Labour Hour rates).

If this view is acceptable, the following suggests itself as a tentative solution.

1. Ascertain the time period which under reasonably normal and settled conditions would represent the useful life of the operational asset to be depreciated.

2. Estimate the normal productivity in terms of output of that asset over the time period ascertained under 1.

3. Calculate the measure of depreciation on a straight line basis having regard to *both* the factors at 1 and 2, regulating the time factor in 1 by the output factor in 2 so that the final arithmetical calculation is a simple one based on time ; nevertheless, it is important to recognise that this calculation is simultaneously related to normal output.

4. Quicken the measure of depreciation above the straight line calculation in proportion as output rises above the normal level estimated at 2, and retain this quickened basis during the time that productivity continues above normal.

5. Do not slacken the measure of depreciation at any time below the straight line calculation notwithstanding the circumstance that output may have fallen below the normal level estimated at 2.

At a time when so many enterprises are faced with the problem of accelerated amortisation it is pertinent to observe the following quotation from the Report of the League of Nations Delegation on Economic Depressions, Part 1 : " The post-war problems created

by the construction of war plants will be particularly serious if provision is not made to allow producers to amortize their plants adequately during the war. If, in the interests of national revenue, amortization rates are kept low, so that at the end of the war the unamortized capital value of the plant greatly exceeds its capital value as determined by the income it can earn in the production of peace-time goods, a powerful factor of dislocation will have been created." (*The Transition from War to Peace Economy*, League of Nations, Geneva, 1943, p. 36.)

We put forward this quotation without further comment, and we close this discussion by urging an output rate which shall be continually tested against and referred back to a fundamental straight line calculation which has been constituted on a " temporal " and " use " basis, the underlying conception of which is one of normality.

Company Law Amendment Committee

Summary of Minutes of Evidence—I

For the convenience of readers, we have attempted to summarise below some of the main points brought out in evidence before the Company Law Amendment Committee, on September 17, September 24, and October 1. The subject matter is, however, extremely detailed and reference to the actual Minutes of Evidence is obviously desirable where possible.

The Registrar of Companies

On the first day, evidence was heard from Mr. P. Martin and Mr. P. J. Rose, C.B., Registrars of Companies in London and Edinburgh respectively, both of whom had submitted memoranda. The main heads of Mr. Martin's memorandum dealt with restrictions on the use of names, the formation of private companies and their conversion into public companies, voluntary winding-up, moribund companies, fees and lists of members.

Regarding the use of names, Mr. Martin's memorandum suggests that the existing law does not go far enough in imposing restrictions. For example, there is a ban on a name identical with that of an existing company but not with that of an existing industrial and provident society. In evidence, Mr. Martin pointed out that if, for instance, a company should wish to use the initials " T.U.C." it would be difficult to turn it down under the provisions of the Act. It was also brought out in questions that under the existing law there would be no power to refuse registration of a name, even if there was a risk of confusion with trade marks.

Discussing Mr. Martin's suggestion that every name should be subject to the approval of the Board of Trade, the chairman asked whether this might not be giving a rather wide power to a Government department. His questions also brought out the point that unless rules for the guidance of the Department were tabled in Parliament—which Mr. Martin felt would not work well —the Courts would have no principles on which to decide appeals. It was further brought out later that if the Department's attitude changed from time to time, it might give rise to a feeling of grievance amongst people who were refused at one time and found that registration was granted to others later on. Replying to a question, Mr. Martin felt it would work quite well to allow people to reserve a name for a certain limited period, perhaps on payment of a fee.

On the formation of private companies, Mr. Martin's memorandum suggests that the actual promoters should be required to reveal themselves and make a declaration of their immediate purpose. While agreeing that there could be nothing to bind the promoters to carry out their intention exactly, Mr. Martin suggested in evidence that it would help to prevent the formation of companies with very wide objects, whose papers are signed only by persons who are quite obviously clerks. The chairman suggested that a more effective method of dealing with this evil would be to find a means of getting rid quickly of moribund companies which had not commenced business within a specified time. Questioned regarding his suggestion that one should try to differentiate in order to distinguish between trading companies and bodies not formed for financial gain, such as the nominee companies of banks or professional and trade associations, Mr. Martin agreed that it would be difficult to draw the dividing line. In later questions Mr. Wilmot brought out the point that there is nothing at the moment to encourage anybody who really seeks only corporate status to refrain from asking for limited liability, and suggested that such an innovation would be a very good idea. It was also brought out in questions that large numbers of private companies do not file their Annual Return, and that this offence is either not followed up or prosecution can take place only with a very considerable time-lag.

To encourage the liquidation of moribund companies, Mr. Martin had suggested that a deposit might be required on incorporation returnable to the liquidator on his appointment, adding that the sale of registrations, at present permitted, had something of the same effect. It was also suggested that directors should be required to furnish a certificate that a company was still active or that there was otherwise a good reason for continuing its existence. In evidence, Mr. Martin suggested that almost anything would provide sufficient reason, saying : " For my part, I should be quite satisfied if I knew someone was interested in keeping the company alive." This certificate, it was suggested, should accompany the Annual Return, to be made fourteen days after the anniversary of the company's formation, the Annual Return itself to be simplified, possibly by omitting the list of members. Questions brought out that lists of members are often inspected, that London is the most convenient place for searches and that it is desirable the information should be centralised rather than be available only from the companies concerned, who might obstruct search.

The Scottish Registrar

Mr. P. J. Rose, C.B., in his evidence, said that he agreed generally with what Mr. Martin had said. In relation to the trade mark question, it might be a little difficult if the Registrar in Scotland had in every case to refer to the Trade Marks Register, 400 miles away, Instead, he suggested that the onus might be put upon the applicant, to see that his proposed name did not conflict with an existing trade mark. Questions brought out that in practice this was closely linked with the proposal

to give the Board of Trade discretion to refuse registrations. Mr. Rose doubted whether power of appeal to the Courts against the Department's decisions would be really necessary, on the ground that a refused applicant is not being deprived of a vested interest but is asking for something like a vested interest to be conferred on him, adding " the refusal of that does not seem to me to be a matter of drastic administrative action by the Board of Trade." Questioned regarding the use of the word " University," Mr. Rose agreed that the Universities could be protected by putting the word into Section 17(2)(b), but pointed out the limitations of giving protection in this patchwork fashion. " In a few years' time you may find there is some other reputable body whose interests are being encroached upon."

On the subject of " dummy companies," Mr. Rose was asked what were the concrete steps he had in mind for ensuring that companies had " a little more substance in their formation." In a series of questions, the chairman brought out that it would be a matter of requiring a minimum amount or a minimum percentage to be subscribed for in cash, or of requiring from the promoters or directors an undertaking to subscribe for a certain amount of capital. This would raise the question of investigating the financial stability of the persons giving the undertaking, which Mr. Rose felt would be rather an onerous obligation on the Registrar. Alternatively, if a deposit were required, this, to be of any value, would have to be substantial in relation not to the nominal capital but to the estimated turn-over, which would be very difficult to estimate. The probable result would be that businesses would not be started or would have to be carried on as a partnership without incorporation. The desirability of this was recognised to be a matter of policy.

The Official Receiver in Companies Liquidation

On the second day the Committee took evidence from Mr. H. P. Naunton, D.S.O., Official Receiver in Companies Liquidation, who had submitted a memorandum dealing with private companies, debentures, winding-up and prosecutions. To prevent abuse of the provisions of the Companies Act relating to private companies, the Memorandum suggests that it is worth consideration whether the minimum number of members of a private company should be increased from two to three or five ; that no company should be incorporated with a nominal capital of less than £2,000 ; and that a statutory deposit should be made of, say, 10 per cent. of the minimum capital, the percentage falling as the amount of nominal capital is increased. Regarding the number of members, Mr. Naunton agreed in evidence that the promoter could always secure the extra number of members by getting nominees, but suggested it would be much more difficult to get so many. He agreed also that a statutory deposit might increase the risk that the company would either borrow on debenture or would have to default. Replying to Sir E. Hodgson, he also agreed that such a deposit might be a very minute proportion of the company's actual debts at any time, and approved the suggestion that it might be sufficient simply to ensure that a company proposing to start business was in possession of cash or convertible assets of a stated amount, though later questions brought out the point that even if the Registrar did satisfy himself that the company had a certain amount of available capital, this would only be momentary. Since the main object of his suggestion was to get at the company formed with liquidation in prospect, Mr. Naunton approved the idea that the deposit provisions might apply only for a limited period until the company was a going concern.

A series of questions were asked regarding the view expressed in Mr. Naunton's memorandum that prosecutions should be instituted in all cases where a criminal offence had been committed, irrespective of whether the matter was one of general public importance and of whether the party defrauded could afford to institute proceedings himself. In evidence, he instanced cases where prosecutions are not undertaken because the Director of Public Prosecutions or the Board of Trade take the view that the persons damaged can afford to take proceedings themselves if they think fit.

The Senior Official Receiver in Bankruptcy

The next witness was Mr. Leslie Arthur West, Senior Official Receiver in Bankruptcy, whose memorandum dealt with restrictions on the use of names, private companies, register of members and debenture holders, remuneration of directors, and the investigation of affairs of companies. A great amount of the work of the bankruptcy examiner arises, he points out, from the power of individuals " to turn themselves into private companies " for dishonest purposes. He therefore suggested a minimum paid-up capital of £500, a deposit of 10 per cent. of the nominal capital, and the filing of a balance sheet certified by an accountant of standing when a company is registered to take over an existing business or assets. Unlike Mr. Naunton, Mr. West would like the deposit to be available only with the leave of the Court and not merely earmarked with the company. Questions brought out the point that under existing law there is practically no disqualification for acting as auditor to a private company. In speaking of an accountant " of standing," Mr. West did not have in mind that the Board of Trade should form a panel of accountants, but agreed that it would be enough if the Department had a list of recognised bodies of accountants.

In his memorandum, Mr. West had suggested that in the event of a winding-up, contributories should be liable to contribute towards the liabilities to an extent sufficient to provide 10s. in the pound for the unsecured creditors. Questions brought out that this might cause certain hardships unless the liability were to subsist only for, say, two years. A further suggestion was that if a shareholder became bankrupt, the Official Receiver should be entitled to sell his shares to anyone and at any price. Mr. West agreed it might be sufficient to have this power only if the shares had not been purchased within a period of, say, one year by the family or whoever was entitled to buy them. There remained the difficulty that if shares were sold to the public at large, a company might cease to be a private company. In reply to a question, Mr. West stated that in a bankruptcy, the list of shareholders in the Annual Return often provides considerable information as to dealings in the shares. On the possibility of limiting directors' remuneration to prevent excessive drawings, the Chairman expressed doubt whether legislation would be practicable. A further series of questions dealt with Mr. West's suggestion that there should be wider powers to hold public examinations of directors in certain circumstances, the Chairman asking at one point whether one should not instead strengthen the powers given to the Board of Trade under Section 135 to appoint an inspector.

The Chief Registrar of Friendly Societies

On the third day, the Committee examined Sir John Fox, O.B.E., Chief Registrar of Friendly Societies. Sir John pointed out that various Acts gave him power to prescribe the form of accounts for the type of business under his supervision, and agreed that the analogy in the case of companies would be for the Board of Trade to have

similar powers. The form of accounts was not specified by rules or for individual societies; the half-a-dozen forms under the Industrial and Provident Societies Act fit all the businesses conducted under that Act. The form of balance sheets is designed to trace malpractice or the non-disclosure of facts which ought to be brought to light. The examiners would not query a statement which led them to believe that fixed assets were undervalued by reference to present market prices, unless they had reason to suspect that hidden reserves were being manipulated for some wrong purpose. Questions brought out the point that such items as goodwill do not arise in connection with businesses registered as friendly societies. He saw no reason why private companies should not be required to publish accounts.

On the appointment of public auditors, Sir John stated that the number of unqualified people on the list is now very small. At one time the list was limited to members of the Chartered Institute and the Incorporated Society, but other bodies had pressed for recognition, and Certified Accountants were now eligible. In reply to questions, Sir John expressed the view that as the State grants the privilege of trading with limited liability, the State should take the responsibility of auditing the accounts, as is done in the National Health Insurance Audit Department. As a second best, he would like a panel of auditors nominated by the Board of Trade, and as third best to ensure that auditors are persons able to undertake an audit, while giving them a right of appeal to the Board of Trade if they were being turned out of office for doing their duty, as had sometimes happened.

He would favour giving the Board of Trade similar powers to those which he himself possessed of moving without prompting by shareholders, debenture-holders, or anyone, and said it would also be a tremendous advantage if an inspector had power to require any person to give evidence who could throw light on the matter under inspection. Where an inspection is made, the Report should in the witness's view be sent to the shareholders interested. In his memorandum, Sir John had suggested that the duty of the auditor is to see that the directors are carrying out their duties properly. Amplifying this in evidence, he explained that in his view they should call the attention of the shareholders to anything reckless or improper, using this word in the wide sense. Under the Acts administered by the Registrar of Friendly Societies, the auditor has to report not only that the accounts are correct, but also where they fail.

Replying to questions, Sir John stated that he had experienced no difficulty in defining a bona fide co-operative society for purposes of the Prevention of Fraud Act; general principles had been laid down for the guidance of intending applicants.

Accounting Principles

The Council of the Institute of Chartered Accountants makes the following further recommendation to its members on certain aspects of the accounts of companies engaged in industrial and commercial enterprises. Whilst it is recognised that the form in which accounts are submitted to shareholders is (subject to compliance with the Companies Act) a matter within the discretion of directors, it is hoped that this recommendation will be helpful to members in advising, in appropriate cases, as to what is regarded as the best practice.

VI. Reserves and Provisions

A true appreciation of the financial position of a company as disclosed by its balance sheet may be rendered difficult or even impossible owing to lack of information as to the extent of undisclosed reserves and to insufficient distinction being made between (*a*) free reserves retained to strengthen the financial position or to meet unknown contingencies; (*b*) capital reserves or other reserves not normally regarded as available for distribution as dividend; (*c*) provisions for known contingencies; and (*d*) provisions for diminution in value of assets in excess of normal or estimated requirements.

The terms "reserves" and "provisions" are commonly regarded as interchangeable. Accounts would be more clearly understood if the term "reserve" were applied only to reserves which are free, and the term "provision" were confined to amounts set aside for specific requirements.

Unless the amounts involved are stated, the trend of profits may be obscured by transferring amounts to or from undisclosed accounts of the nature of free reserves, by charging abnormal provisions, or by utilising provisions no longer required.

Recommendation

It is therefore recommended that:

(1) The following distinction should be made between reserves which are free and those in the nature of provisions for specific requirements; the latter should preferably be described as "Provisions":

(*a*) The term "reserve" should be used to denote amounts set aside out of profits and other surpluses which are not designed to meet any liability, contingency, commitment or diminution in value of assets known to exist as at the date of the balance sheet.

(*b*) The term "provision" should be used to denote amounts set aside out of profits or other surpluses to meet:

(i) specific requirements the amounts whereof can be estimated closely; and

(ii) specific commitments, known contingencies and diminutions in values of assets existing as at the date of the balance sheet where the amounts involved cannot be determined with substantial accuracy.

(2) Reserves, as defined in (1) (*a*) above, should be disclosed in the balance sheet.

The term "Reserve Fund" should only be used where a reserve is specifically represented by readily realisable and earmarked assets.

Where two or more reserves are retentions of distributable profits available for general use in the business and none of them is created in accordance with statutory requirements or in pursuance of any obligation or policy, the subdivision of such reserves under a variety of headings is unnecessary. Capital and other reserves not normally regarded as available for distribution as dividend, should, however, be separated from those of a revenue nature, the latter group to include any undistributed balance, or, by deduction, any adverse balance on profit and loss account.

(3) As a general principle "Provisions" as defined under (1) (*b*) (ii), should be disclosed in the balance sheet under one or more appropriate headings. Only in circumstances where disclosure of the amount of a particular provision would clearly be detrimental to the interests of a company should

it be included under another heading, for example "Creditors"; the fact that such heading includes "Provisions" should then be indicated in the narrative.

Where practicable, fixed assets in existence at the date of the balance sheet should be shown at cost, and provisions for depreciation and for diminution in values should appear as separate deductions therefrom.

(4) Subject as in (3) above in regard to provisions the disclosure of which would be detrimental to the interests of a company, where reserves and provisions are created or increased, the amounts involved, if material, and the sources from which they have been created or increased, should be disclosed in the accounts. In all cases the utilisation of reserves, and of provisions proved to have been redundant, should be disclosed in the accounts.

TAXATION

Income Tax (Employments) Act, 1943

The Wage-earners' Income Tax Bill has now been passed under its new title. As accountants, we find it unsatisfactory, inasmuch as so much is left in the air. The Chancellor has stated that transitional provisions will be dealt with in the next Finance Bill, and that the extension of the Act to persons earning more than £600 will also be dealt with in that Bill or in a special one. Moreover, we still await the Regulations and the much-criticised Tax Tables which the Parliamentary Secretary said would be nearer 1,000 pages than 5,000. We hope that copies of the complete tables will be available for accountants' offices. With the thousands of copies that will be required, the few necessary for such distribution will make little difference to the paper requirements and their possession will be essential to checking clients' tax deductions.

At the time of writing, one very important point in the Act has received no publicity, namely that it only applies (apart from manual wage-earners and those whose wages are calculated by reference to a period less than a month) to emoluments if the person in receipt of them satisfies the following conditions:

(*a*) His emoluments are assessable under Schedule B;

(*b*) The total emoluments from all employments so assessable do not exceed £600 (excluding overtime); *and*

(*c*) The employment or employments together take up his full time.

It appears, therefore, that, at least for the time being, persons other than those who can perhaps be called "weekly wage-earners" will not get the benefit of pay-as-you-earn where they are not full-time employees. It is to be hoped that when the scheme is extended to those earning more than £600 a year, the whole of Schedule E will be included, otherwise peculiar anomalies will arise.

Civil servants and railway workers are now included, though without tax "forgiveness," but members of the Armed Forces are not. The latter, of course, will continue to have tax deducted over the fiscal year, but will continue on the preceding year basis of assessment.

The Chancellor apparently needed time to think out the remedies to meet possible "wangles" between Schedule D and Schedule E, such as can arise in the case of one-man companies, before bringing in legislation for extending the system; but he has promised that the necessary legislation will have effect from April 6 next. Parliamentary procedure apparently prevented a private member from moving an amendment in view of these safeguards being required.

We do not want to labour our dislike of the Tax Tables, but cannot help quoting Mr. Douglas' apt remarks: "It is a system in which there is a very great liability to error, owing to the complicated nature of the calculations and of the tax tables. Some of those errors may be of a cumulative character, going on accumulating until the end of the period. That arises largely out of the fact that the apparatus devised for carrying on this system is very different from the ordinary methods of accounting and is based on a series of tax cards which are not reconcilable with the books of the business and do not lend themselves to easy and periodical balancing. In this time of war, when the shortage of man-power is most acute, it is serious that no effort should be made to try to put into operation a system involving less expense and trouble."

Many taxpayers are against the extension of pay-as-you-earn owing to the fact that the change in the basis of assessment from the "preceding year" to "actual" will involve them in a bigger liability on increasing pay. While we sympathise with the drain on their pockets, we must point out that for the first time they will be paying what they really ought, while the hardship hitherto felt in cases of decreasing pay is done away with. As Mr. Benson said: "The objection to assessment on the previous year's earnings was that there are very large variations in wages between one year and another. . . . The overwhelming argument in favour of pay-as-you-earn is the fact that sooner or later there will be a very large number of people who are now in industry going out of industry. In the post-war period of industrial adjustment there would be vast masses of tax which we could not collect and it would be impossible for the Board of Inland Revenue to decide who should be forgiven tax and who should not."

In the case of those who would never have been in the class of not being able to meet the liability, despite its hardship, it will be a relief to know that when employment ceases either by retirement or by death, there will be no arrears to be met out of smaller income or out of the estate. The civil servants asked to be brought into the scheme just for that very reason, i.e. to get rid of what the Chancellor referred to as overlapping payments.

It is likely that an amendment will be necessary in the case of married couples where the wife is working. The reduced rate relief being given to both may result in relatively considerable under-deduction. While the Treasury have leant towards under- rather than over-deduction, the general trend of opinion appears to lean the other way.

At this point, we think it well to leave the Act. The next Bill must inevitably be of greater interest (and size), and by then we shall have had experience of the working of the present provisions. A revolutionary change is being brought about in the inevitable British way—piecemeal. It is a pity that a little more courage and progressiveness could not have been shown and a new tree planted instead of grafting on new branches to the existing tree.

Taxation Notes

Working Proprietors Standard

As is now well known, the Revenue normally give effect to the size of the business by adding 6 per cent. on the average capital employed in excess of £5,000 per working proprietor. A new development of this is reported, which may assume considerable importance. The Board have decided that, although normally the average capital for this purpose shall be computed by reference to the cost of the assets and no account should be taken of the value created by a war-time scarcity, yet if it can be shown that the value of the assets as a whole was substantially greater at the time at which they were acquired than the price at which they were taken over, the Board might be prepared to have regard to the value of the assets at the time at which they were acquired rather than their cost price.

Directions made by the Board of Referees under Section 13, Finance (No. 2) Act, 1940 (Provisions as to Mines, Oil Wells, &c.)

The Board of Referees have directed in relation to the classes of trades or businesses set out hereunder that the percentage rates prescribed by Section 27 of the Finance Act, 1940, and the statutory percentages prescribed by subsection (9) of Section 13 of the Finance (No. 2) Act, 1939, shall be increased by the percentages specified below :

Class of trade or business	*Additional percentage*
Copper Mining in Northern Rhodesia ...	3·65
Zinc and Vanadium Mining in Rhodesia ...	3·25
Gold Mining in Kenya	4
Oil getting in the Attock and Rawalpindi area of India	4
Getting of iron-ore in Sierra Leone	2·25
Asbestos mining in Southern Rhodesia, Swaziland and South Africa	3·56
Gold mining in Venezuela	4
Quartz gold mining industry of Southern Rhodesia, and Bechuanaland Protectorate	4

Cost of Uncompleted Contracts

It was decided in *City of London Contract Corporation* v. *Styles* (1887) 2 T.C. 239, that the cost of unexecuted contracts taken over with a business cannot be deducted in computing the profits from the performance of those contracts. The point arises from time to time and students often fail to grasp the reasons behind the decision. These are simple, viz. that the cost of the acquisition of the contracts is a capital expense : it is the outlay to acquire rights, not the acquisition of a floating asset. The following illustration should make it clear :

A. and B. went into partnership, contributing £10,000 each as capital. They took over from X., Ltd., certain contracts partially executed, paying for them the prime cost to date plus 10 per cent., a total consideration of £20,000. It should be obvious that if A. and B. were able to deduct £20,000 from the consideration received on the completion of the contracts, as well as their costs of completing, they would be repaying their capital outlay out of revenue.

Capital Employed

The decision in *C.I.R.* v. *Terence Byron* (1943, T.R. 271) should be noted by all accountants, as it was decided that a building destroyed by enemy action continued to be employed as an asset in the company's business for the purposes of the capital computation for E.P.T. purposes. The case may, of course, go further, but in the meantime, the following *dicta* of MacNaghten, J., are important :

> " It seems . . . that the word ' employed,' as used . . . in connection with the word ' capital,' is not used in a very strict sense, and that the expression, ' capital employed in a trade or business,' has much the same meaning as ' the capital of a trade or business ' and must be so construed," and ". . . If the standard profit suffers no deduction by reason of the fact that the person carrying on the trade or business does not choose to use a particular asset, it would seem unreasonable to reduce the standard profit because the asset has become unusable owing to enemy action."

Recent Tax Cases

By W. B. COWCHER, O.B.E., B.Litt., Barrister-at-Law

Schedule E—Managing director—Receipt of percentage of sums received by another company—Assignment of sums to another person—Loan by latter to managing director—Whether assessable income.

In *Parkins* v. *Warwick* (K.B.D., July 13, 1943, T.R. 259), appellant was chairman and managing director of a gold-mining company which in 1936 purchased from a syndicate two mining leases for £50,000, payable over five years. By the articles of the first company, appellant's remuneration as managing director was to be fixed by the directors. In September, 1936, the Syndicate wrote to him a letter saying that, in view of their great interest in the gold-mining company and of his having agreed to charge the company nothing for his services as managing director over and above his £100 per annum as chairman, it undertook to pay him 5 per cent. of the moneys received from time to time in respect of the £50,000 sale to the company. In October, 1936, appellant assigned the sums thereafter payable by the Syndicate and, in consideration, the assignee released appellant from a debt of £200 and agreed to lend him the said sums as and when paid by the Syndicate free of interest for five years. Appellant was also to be given an option over certain shares.

The first question in an artificial position was whether the payments agreed to be made by the Syndicate represented emoluments of appellant's office as managing director. He, however, did not contest the point before Macnaughten, J. The second question was whether, as the amounts came to appellant by way of loans, they ought to be regarded as income. As to this, the judge said that the appellant disregarded the channel through which they came. From the Syndicate they passed to appellant as managing director, then from appellant they passed to the assignee, and then from the assignee back to appellant as borrower. Referring to Mr. Justice Channell's judgment in *Smyth* v. *Stretton* (1904, 90 L.T. 756, 5 T.C. 36) he said that it did not occur to that judge that it would be possible for anyone to argue that where the recipient of an emolument had the full right to apply it as he liked he could by any arrangement release himself from the obligation to pay tax. Appellant was free to deal with these emoluments as he liked, but his having done so did not make them any the less assessable. To

an observation by the appellant after judgment, his lordship replied that it had long been held that a valid assignment could be made of a future emolument.

Potentially, the case was interesting and important in its legal aspects; and it is unfortunate that it was not argued by a member of the Bar. Appellant, as managing director of the company, owed no duty to the Syndicate, and, unless its letter of September, 1936, was under seal, the undertaking therein would seem to have been unenforceable. Still, the fact of the payments being voluntary would not, apparently, prevent their being emoluments assessable under Schedule E. Their assignment, assuming the existence of assignable legal rights, raises other questions. If the right to receive future income can be assigned where such income is assessable under Schedule D and it then ceases to be income of the transferor, it would seem equally possible in respect of income assessable under Schedule E. (As regards Schedule D, the judgment of Romer, L.J., in *Dewar* v. *C.I.R.* (1935, 19 T.C. 561) and those in *Paget* v. *C.I.R.* (1938, 21 T.C. 677) may be referred to.) It would seem to make no difference whether the payments were made through the transferor or direct to the assignee. In the former case, he would receive as bare trustee only. Upon the facts as reported, having made the assignment, appellant had divested himself of all right of applying the sums as and when paid.

Sur-tax—Purchase of shares and landed property in name of son—Dividend warrants and cheques received by son—Endorsed in favour of father—Paid into father's banking account or into account of father's company—Payments out of account for premiums on policies on son's life—Assignment of policies to father without consideration—Whether dividends and interest father's or son's income.

The nature of and facts in *Sinclair* v. *C.I.R.* (Court of Session, March 11, 1943, T.R. 277), apart from those of a minor issue, are sufficiently stated in the heading. The Revenue had made a series of assessments upon appellant for the years 1931-2 to 1938-9 in respect of the income, and, upon appeal, the Special Commissioners had affirmed them, holding that the son was a mere nominee. The court unanimously affirmed their decision, holding that there was ample evidence for it.

One very interesting point arose in the case which the court found it unnecessary to decide. It was whether the Crown was entitled to give in evidence a document not duly stamped. Lord Fleming pointed out that although the statutory prohibition was intended to safeguard the Revenue it was peremptory in character.

E.P.T.—Capital employed—Destruction of premises—Should cost thereof be thenceforward excluded in computing capital employed?—Finance (No. 2) Act, 1939, Sections 13 (3), 14 (2); 7th Schedule, Part II, para. 1.

In *C.I.R.* v. *Terence Byron, Ltd.* (K.B.D., July 20, 1943, T.R. 270), the General Commissioners and Macnaghten, J., answered in favour of the taxpayer. His lordship held that "capital employed in" had much the same meaning as "capital of," and said that "a debt due" was no doubt an "asset," but could not in ordinary parlance be described as "employed" before payment. He saw no distinction between the value of an asset destroyed and of one temporarily unused so far as "employment" was concerned. The Court of Appeal is to consider what is a very abstruse problem.

E.P.T.—Company controlled by directors—Whole-time director owning more than 5 per cent. ordinary share capital in standard period—None in chargeable period—Should remuneration be added back in standard period but allowed in chargeable period?—Finance (No. 2) Act, 1939, Section 14 (1); F.A., 1940, Section 33 (5); F.A., 1941, Section 39.

In *C.I.R.* v. *Ash Brothers & Heaton, Ltd.* (K.B.D., July 21, 1943, T.R. 269), this important point had been decided against the Crown by the Special Commissioners. They were upheld by Macnaghten, J. The Crown claimed to apply the "like with like" principle; but it was held that para. 10 (1) of 7th Schedule (as revised by F.A., 1940, Section 33 (5)) was too plain. After the sale of the shares its provisions did not apply. Presumably, had the director not only sold his shares but resigned and been replaced by a "not more than 5 per cent." stranger, the Crown would not have raised any question. If so, it is hard to see the distinction.

Income tax—Annuities under will—Actuarial values in excess of value of estate—Income of estate insufficient—Annuitants therefore entitled to divide estate between them—Whether payments to annuitants in respect of annuities or instalments of residue.

In *C.I.R.* v. *Lady Castlemaine* (K.B.D., July 27, 1943, T.R. 275), the Special Commissioners and Macnaghten, J., held that the payments made to respondent on account of her annuity at a time when it was not known that the estate was deficient did not abrogate or affect her rights. They had to be regarded as capital payments. The Crown's alternative claim under F.A., 1938, Sections 31 to 35 (which revised the law as to residuary income arising during the administration of estates) had not been made before the Special Commissioners, and, not being referred to in the stated case, was disallowed. No doubt, additional assessments will be contemplated.

E.P.T.—Statutory percentage upon increase of capital—Rate determined by whether directors have controlling interest—Directors as trustees jointly holding shares—Whether these shares to be taken into account in determining question of control—Finance (No. 2) Act, 1939, Section 13 (3), (9).

In *J. Bibby & Son, Ltd.* v. *C.I.R.* (K.B.D., July 28, 1943, T.R. 297), Macnaghten, J., affirmed a decision of the Special Commissioners that the shares held by trustees had to be excluded in ascertaining whether directors have a controlling interest in a company. "As trustees they have no 'interest' in the shares and as beneficiaries they have no control." The decision is important and will, it is surmised, be carried farther. There is much to be said for the contrary view because "control" is, fundamentally, a fact. Still, in the present case, if the trustees' shares were excluded the directors did not hold a majority of the remainder. It would have been a stronger case if they had.

Schedule D—Land suitable for development purchased 1931—Additional area purchased 1932 to provide access—No development—Acceptance 1932 of offer for whole—In 1934, purchase and sale of other land—Facts similar—In 1929, testator partner in land development business—Assessments 1932-33 and 1934-35—Whether a trade assessable Case I.

In *Reynold's Executors* v. *Bennett* (K.B.D., July 22, 1943, T.R. 291), the Special Commissioners had confirmed the assessments and Macnaghten, J., held that there was evidence making it a reasonable conclusion. The decision was clearly a finding of fact; but, as the Judge remarked, they "perhaps incautiously did not confine themselves to merely stating the conclusion of fact at which they arrived," but showed how their minds had been made up. The truth of the matter would seem to be that the Special Commissioners are being too hard pressed in these days.

Schedule E—Gifts of money and of savings certificates by employers to employees completing 25 years' service—Whether emoluments of office or employment or only "personal gifts."

In *Weston* v. *Hearn* and *Carmouche* v. *Hearn* (K.B.D., July 23, 1943, T.R. 295), the decision of the City Commissioners against the appellants was affirmed by Macnaghten, J. It appeared that the payments were in accordance with the practice of the employing company; and it was held that they were not "personal gifts" within *Reed* v. *Seymour* (1927, A.C. 554, 11 T.C. 625) and *Cavan* v. *Seymour* (1920, 1 K.B. 500, 7 T.C. 372), but in respect of services.

Sur-tax—Tenant for life—Accumulation of income during minority—Under Section 31 (2) of Trustee Act, 1925 he became absolutely entitled to accumulations on attaining majority, but had he died before then the accumulations were to be treated as accretions to the capital of the trust—Whether appellant was entitled to accumulations of income during minority.

In *Stanley* v. *C.I.R.* (K.B.D., July 28, 1943, T.R. 299), the question arose out of the change in the law made by Section 31 (2) of the Trustee Act, 1925, whereby in the event of a tenant for life dying during minority any accumulations of income were to become capital of the trust and not pass as previously to the next-of-kin. Macnaghten, J., held that, despite this fact, they were still his property and that the sur-tax assessments made upon him on attaining his majority were valid.

Schedule D—Company dealing in real property in London—Assessed Case I on results—Option to purchase estate—Agreement between appellant and H to form company to purchase and develop part of estate in equal shares—Offer to appellant by H for his half interest accepted—Whether profit assessable as arising from trade.

In *Associated London Properties, Ltd.* v. *Henriksen* (K.B.D., July 26, 1943, T.R. 301), the General Commissioners found for the Revenue, and Macnaghten, J., after a remit of the case, held that there was ample evidence to support the finding that the profit arose from the company's trade. It was another case where an unfortunate reason had been given for a finding of fact.

Income tax—Relief in respect of bank interest paid—Whether proviso to Section 36, Income Tax Act, 1918, applies to sub-section (1) as well as to sub-section (2), i.e. whether to interest paid to banks as well as to interest paid to Stock Exchange firms and discount houses—Proviso imposes condition that C.I.R. are to be satisfied that interest paid will be returned for income tax by the lender—F.A., 1915, Section 22; F.A., 1917, Section 15; Income Tax Act, 1918, Section 36.

In *Webb's Executrix* v. *C.I.R.* (K.B.D., July 16, 1943, T.R. 265), it was held that the condition imposed by the proviso to Section 36, which was first imposed when the relief given in 1915, in respect of bank interest alone, was extended in 1917, applied to both limbs of the section. Macnaghten, J., found that it did; and pointed out that in *C.I.R.* v. *Holder* (1932, 16 T.C. 540) Lords Thankerton and Macmillan were of the same opinion.

The condition in the proviso is a very curious one with strange possibilities. In fact, the whole section is marked by inequality and uncertainty. It is worthy of note that the Codification Committee in 1936 declared that the opinions upon the point at issue in the *Holder* case were *obiter*; and they left it open. (Report, p. 213.)

Income tax—Mining lease—Right to withdraw support—Payment as liquidated damages—Whether payments are "rent"—Whether rents in respect of an "easement"—F.A., 1934, Section 21.

Earl Fitzwilliam's Collieries, Ltd. v. *Phillips* (House of Lords, August 4, 1943, T.R. 309), was noted in our issues of February and July, 1942. In the House of Lords the decision for the Crown of the Court of Appeal was affirmed. In the course of the case it was assumed that a right to withdraw support was indistinguishable from an immunity from action for damage; and the question, therefore, was whether the decision of the Court of Appeal in favour of the Crown in *C.I.R.* v. *New Sharlston Collieries, Ltd.* (1937, 1 K.B. 583, 21 T.C. 69), was correct.

SCOTTISH NOTES

Glasgow City Chamberlain

The Glasgow Corporation have appointed Mr. G. B. Esslemont, M.A., B.Com., LL.B., C.A., at present Principal Assistant in the City Chamberlain's Department, to be City Chamberlain. Mr. Esslemont was formerly assistant to Mr. David Ritchie Bishop, F.S.A.A., City Chamberlain, Aberdeen.

Scottish Local Government Reform

The first report of a Committee appointed in 1937, with Sir John Jeffrey as Chairman, to attempt to codify the law relating to local government in Scotland, has just been published.

The Committee is understood to have completed the local government part of their remit, and their report, said to have been ready in August, 1939, has only now been given to the public.

Several matters of considerable importance to the accountancy profession are referred to.

If the Committee's recommendations are adopted, the "Revenue and Expenditure" basis will be adopted for the purposes of all accounts instead of the "Receipts and Payments" basis, where that is at present used. Auditors will be required to report specifically on the administration and organisation of authorities in regard to financial matters and the repayment of moneys borrowed.

Regarding appointments to the office of Treasurer, the Committee suggests that the Secretary of State should have power to prescribe professional qualifications by regulations, which, once made, could be varied from time to time. They think that ultimately every County Treasurer and every Town Chamberlain should be required to have the prescribed qualifications.

Companies Act

The Glasgow Chamber of Commerce recently appointed, at the request of the Association of British Chambers of Commerce, a special committee to take into consideration various suggestions for the amendment of the Companies Act, 1929.

Some measure of control was suggested in the minute restricting the right of a vendor or principal shareholder from taking from a company a debenture for a disproportionately large amount, as compared with the issued share capital, with a floating charge over the whole undertaking, thereby securing to himself a preference as against ordinary creditors. It was also suggested that the Board of Trade Committee should take into consideration the differences between the law of England and the law of Scotland in reference to the creation of securities over movables, such as stock-in-trade and book debts. The floating charge competent under English law, but believed to be invalid under Scots law, placed English businesses in a relatively advantageous position in regard to the obtaining of finance for business purposes, and, while an alteration of the law of Scotland on that point would have effect far beyond the ambit of company law, it should be investigated in the interests of Scottish industry.

FINANCE

The Month in the City

The Trend of Equities

It is well known that in any given situation, Stock Exchange prices tend to react rather too violently in either direction. This swing of the pendulum became apparent again in the middle of last month, when equity prices showed signs of recovery after declining since the beginning of October. The situation which prices were trying to reflect was the possibility that the war might be over sooner than most people expected. The result was a fall in both "war" and "peace" shares, the former for obvious reasons, and the latter because of the feeling that post-war profits might be better in anticipation than in realisation. Prices may now have fallen enough to satisfy this increased feeling of uncertainty; but even if the recession proves as temporary as those which have taken place earlier in the war, it provides some interesting contrasts in timing and composition. Previous recessions have occurred in the first quarters of 1941 and 1942, when there were plausible economic factors to account for them. It is quite understandable that when tax payments and savings subscriptions are at their peak, resources should be diverted from the Stock markets. The past recession, however, has taken place when the seasonal expansion in bank deposits is in full swing, and when all the financial influences would favour a continued Stock Exchange advance. Another difference has been in the trend of individual groups. The decline in "war" stocks, like aircraft and rails, actually began quite early in the year, and for several months there was a "scissors" movement while "peace" securities continued to rise. It is only since October that post-war doubts appear to have affected both categories. The market's behaviour can thus be fairly plausibly explained in terms of expectations of a short war, but it is another matter to justify it. It is clear enough that monetary expansion would favour equities if the controls were removed. But this is just the point about which the investor is in doubt. He would like to know what is to happen to E.P.T., and how far increased peace-time business will be allowed to raise distributable earnings. These uncertainties affect even shares in the obvious recovery groups, like buildings, stores and textiles; it is a matter of opinion how far they should be reflected in prices. Industrial equities, of course, have only these general doubts to contend with. For concerns falling into the utility class there are the additional possibilities of political attention, but in the case of Home Rails, the market has found some reassurance in Lord Leathers' opinion that the railways should be safeguarded either by nationalisation or by being allowed to earn a reasonable profit. Both the gas and electricity industries also seem conscious of the need for securing their position, and have published plans for facilitating a process of rationalisation under existing conditions of ownership. Among overseas securities, Argentine rails recently derived some encouragement from the news that a committee has been appointed to investigate the position of the British-owned railways, and Brazilian Government bonds have benefited from the announcement that a settlement of the external debt is expected in the near future.

Four Share Issues

In the past few weeks an unusual number of industrial companies have been permitted to make offers of new capital to existing shareholders. Three of the companies concerned, Dorman Long, Richardsons Westgarth, and Horseley Bridge & Thomas Piggott, fall into the heavy engineering category, while the remaining one, Joshua Hoyle, is a leading cotton spinning and manufacturing concern. In the case of Horseley Bridge, the additional capital is required for financing an increase in the company's business, but in every other instance the issue of ordinary shares is a means for the repayment of debenture capital. This rearrangement of capital structure has evidently been considered so important that in at least two instances the offer has been made in such a way that there will be no reduction in the cost of servicing the capital, assuming the maintenance of the ordinary dividends. The nature of the operations suggests that the boards have been looking backwards to a time when conditions of depression made fixed charges a particularly heavy burden. The market, on the other hand, is inclined to look forwards, and is expecting prosperous conditions in the textile, and even the heavy engineering industries, after the war. In these circumstances, it is not surprising that the offers were received with mixed feelings, and that some of the "rights" have been dealt in at very small premia. The offers were, of course, made at an unfortunate time of falling prices, but the result might have been much the same at any time. The expectation of rising profits during the post-war recovery period has led the investor to favour companies with "highly-geared" equities, and any dilution of the ordinary share capital naturally diminishes these attractions. On the longer view, however, there is much to be said for this preference for financing mainly by means of ordinary shares. It means a smoothing out of the effects of both boom and slump on equity dividends.

Great Universal Stores

In asking for more information about the affairs of Great Universal Stores, the Stock Exchange Committee has recently kept up its reputation for watching the interests of the investing public. Their action has, of course, far wider implications than the specific case which prompted it. There is still a lot of hard thinking to be done about the duties of directors, and how far these duties should be embodied in legislation or imposed by the sanctions which can be brought to bear by private institutions like the Stock Exchange. The pros and cons of this particular case have been widely discussed, and without going back over the details, there are a number of points of principle which deserve wider consideration. The basic fact was that directors who had interests in competing concerns had sold these interests to Great Universal Stores at a profit to themselves before the approval of shareholders had been sought. The details of these transactions supplied in a circular show that the profits to the vendors could hardly be described as large. In the absence, however, of disclosure of the names of the companies concerned and the value of their assets, it is difficult for shareholders to judge whether the transactions were suitable from their company's point of view. Apart from these points which arise out of the information given by the company, several wider issues emerge. The transactions themselves recognise the undesirability of directors holding interests in competing concerns, but in special circumstances of this sort should not the sales have awaited shareholders' approval and have been based on even fuller disclosure than has yet been supplied?

Points from Published Accounts

False Modesty v. Brutal Frankness

Quite the most interesting set of accounts, from an accounting point of view, that have been published for many a long day are those of Clark, Son and Morland. The chairman claims that these show the earnings experience with " exemplary candour and brutal frankness " ; and certainly they are unique in that the directors' report displays the legal position in respect of taxation. The profit and loss account reveals a net profit of £3,729, after providing £7,385 for depreciation, £35,508 for taxation, and £6,000 for trade investments reserve. The report declares that during the incidence of E.P.T., and while income tax is at 10s. in the £, the profit, after providing for tax, is practically stabilised at £12,000. The difference between this sum and the published figure of £3,729 is accounted for by the reserve against trade investments, and by a net sum of £2,271 representing depreciation charged in excess of Inland Revenue allowance ; the gross sum was £3,000, but, against this, credit has been taken for minor adjustments of £729 on income tax computations. The chairman's statement carries the story further back, for it gives a seven-year record of net earnings as agreed for the purposes of income tax. Mr. H. F. Scott Stokes's comment is that this " flatters our performance, in that we have at all times felt it necessary to make substantial additional reserves for depreciation beyond the Inland Revenue scale, say £2,500 a year extra, and other small reserves which have been disallowed by the Inland Revenue. . . . It may flatter us, but it is the only figure which is based on known standards, and cannot be questioned. Any other figure of ' profit ' is very much what you choose to make it ! " Questioning the worth of false modesty, Mr. Scott Stokes says : " I am no longer quite sure that the persistent understatement of one's own performance is quite wise. It is not even strictly truthful." Combined with a statement of the company's depreciation record—the amount allowed by the Inland Revenue in the 17½ years to June 30, 1942, was £55,459, whereas the amount charged against profits over the same period was £80,913—these opinions do indeed reach down to fundamentals. This is a frontal assault on orthodoxy. There is no little significance in a company's going out of its way to illumine the meaning of its own profit figures by reference to the figures agreed for tax purposes. But it is worth stressing, perhaps, that the latter are not necessarily a precise measure of " real " profits ; these have still to be defined.

Income Tax and Net Profits

As it happens, the importance of provisions over and above the allowances sanctioned by the tax authorities is emphasised by the accounts of two companies that have recently reported. Such provisions modify the " fifty-fifty " relationship between income tax and bare net profits, and the position is complicated by the increasing tendency to accumulate reserves for future taxation by annual allocations from profits. At the least, however, some explanation ought to be offered where the disparity is very great. This is the case with Bristol Aeroplane, which returns a net profit of £282,291, after providing £730,000 for income tax. From this bare net profit £100,000 is added to general reserve, so that on the face of it, dividend disbursements must be very modest in relation to the profit as agreed for tax purposes. The other example is afforded by the United Steel Companies. Here the " reserve for income tax on the profits of the current year " is £1,290,000, whereas the bare net profit is only £459,579, reduced to £408,506, by taking £51,073 to reserve for debenture stock redemption.

Burberrys' Assets Position

The balance-sheet of Burberrys shows an assets total of £1,919,685 to be represented as to £446,780 by goodwill. A further £263,187 is accounted for by the book value of the whole of the capital of H. J. Nicoll and Co. Until this year it has always been an open question whether, and to what extent, a further goodwill item was concealed in the valuation placed upon this interest in the subsidiary. The question has now been answered, so far as it lies in the directors' power to do so, by including with the parent company's own accounts a print of the balance-sheet and profit and loss account of H. J. Nicoll and Co. Two items in this deserve special attention. Goodwill is entered at £1,231 and leasehold premises at £10,705. Excluding these, the net assets amount to £113,064. But the lease of the Regent Street premises, which cost £54,866, has 48 years still to run and was valued in 1919 at £132,000. The present value may well be greater than the residual figure placed upon it in the balance-sheet. What intrinsic worth can be placed upon the subsidiary's goodwill is, however, another matter, for while the company earned £23,426 net in the past period its career has, in the chairman's own words, been a chequered one. This has to be borne in mind in noting the statement that the H. J. Nicoll profit is equivalent to 8.8 per cent. on the £263,187 book value of Burberrys' investment in that company. Incidentally this net value is revealed, for the first time, in Burberrys' own accounts as having been determined after writing off amounts of £176,896. The picture obtained from the accounts is inevitably not a firm one, but it is much clearer than before.

Horlicks

In the Horlicks balance-sheet creditors and credit balances, amounting to £281,439, are described as " including provision for income tax and Excess Profits Tax on profits to date after deducting holding of tax reserve certificates." This method of including tax provisions at a net sum is doubly objectionable. It conceals the amount held in tax reserve certificates, thus running counter to what has now become established accounting practice. And it leaves shareholders with no true idea of the company's total current liabilities. Remembering that an increasing number of companies are segregating their tax provisions from general creditor balances, and even dividing them into provisions against the accrued legal liability and reserves against future liability, there is a strong case for modifying the practice followed by Horlicks.

Odeon Theatres

Last month, in commenting upon the accounts of Odeon Theatres, we referred to an earlier note on Gaumont-British and described Odeon as " another member of the same group." The intention was to emphasise that both companies came within the ambit of the Rank interests ; but it has been represented to us that the impression might be left that Odeon is a member of the Gaumont-British group. In fact, of course, there is no financial link between the two companies, though Mr. J. Arthur Rank is chairman of both boards, and we are happy to make the position quite clear.

LAW

Legal Notes

COMPANY LAW.

Meetings—Quorum—Proxies against Resolution—Chairman's Duty to demand Poll.

Reported decisions on the duties of chairmen at meetings are few. The matter is important, because the chairman is usually highly interested in the result of voting by the meeting, and his conduct of the meeting over which he presides must be fair to all concerned. In *The Second Consolidated Trust, Ltd.* v. *Ceylon Amalgamated Tea and Rubber Estates, Ltd.* (1943, 2 All E.R. 567), Uthwatt, J., decided that on the facts of that case and the true construction of the trust deed then operative, the power of the chairman to demand a poll was not a personal right to be exercised according to his wishes; he had no unlimited discretion as to the manner in which he might exercise that power. The duty of a chairman was to ascertain the sense of the meeting upon any resolution properly coming before it. The power to demand a poll was the power possessed by the chairman which was to be exercised or not according to his decision whether it was necessary to exercise the power in order to ascertain the sense of the meeting. It was a power directed towards enabling him to carry on the meeting for the purpose for which it was convened. In the particular circumstances, particularly as the persons present did not form a quorum, the chairman ought to have demanded a poll and used the proxies. The defendant company wished to alter the conditions under which its debenture stock was held, pursuant to the provisions of the trust deed securing that stock. In order to do so it was necessary to pass an extraordinary resolution by a three-quarters majority at a duly-convened meeting at which the holders of a clear majority in value of the stock were present in person or by proxy. The trust deed further stated that on a show of hands a stockholder present only by proxy should have no vote. The meeting was duly convened and with the notice convening it, a form of proxy was sent to all the stockholders whereby they could indicate the specific manner in which they wished their votes to be used. At the meeting, the 14 persons present in person were unanimously in favour of the resolution, but they did not constitute a quorum unless the proxies were counted in. The proxies were such that, if a poll was demanded and the proxies used for the purpose of the vote, the resolution could not be passed. The resolution was passed by the stockholders present in person. The chairman, aware of all the facts and acting *bona fide*, did not demand a poll. The plaintiff stockholders contended that the meeting was not duly constituted, and, alternatively, that the proceedings were irregularly conducted, and that the resolution was invalidly passed. The Court held, for the reasons set out above, that the resolution was not properly carried. Uthwatt, J., also stated that, in addition to his duty to exercise his power to demand a poll, the chairman would be under a duty in law to exercise all the proxies which he held as chairman in accordance with the instructions which they contained.

EXECUTORSHIP LAW AND TRUSTS

Charities—Bequest to Unincorporated Society to be used for Specified Purpose.

In *Re Price* (1943, 2 All E.R. 505), by her will dated June 13, 1940, the testatrix directed that one half of her residuary estate should be held on trust for the payment to the Anthroposophical Society to be used at the discretion of the chairman and executive council of the Society for carrying on the teachings of the founder, Rudolf Steiner. The testatrix died in July, 1940, and the Society contended that the gift was valid on three grounds, alternatively: (1) that it was an absolute gift to the Society; (2) that there was nothing to prevent the Society from expending capital as well as income on the particular purpose declared in the will; (3) that it was a valid charitable gift. Cohen, J., held: (1) on the construction of the will, the members of the Society were not free to expend the gift as they thought fit. The Society was bound to apply the gift only for the purposes expressed in the will, although they might expend capital on those purposes; (2) as both capital and income could be so expended, there was no infringements of the rule against perpetuities; (3) the gift was a valid charitable gift.

Will—Option to Reversioner to purchase after death of Life-tenant—Sale by Life-tenant.

In *Re Armstrong's Will Trusts* (1943, 2 All E.R. 537), Cohen, J., decided that an option to purchase land given in respect of settled land may be exercised although that land has been sold by the life-tenant under the statutory powers. In such a case the option is exercisable in respect of the capital money and investments representing the land. By his will made in 1899, the testator gave certain lands to his wife for life and directed that, after her death, the lands should fall into residue. He gave his son H. an option, exercisable only within 12 months of the death of the widow, to purchase the land in question at the price of £5,000. The testator died in 1900. The land in question, described as "Steetley Farm," at the testator's death comprised 200 acres of land which contained valuable deposits of limestone, capable of being worked. In exercise of her powers as life-tenant, the widow sold part of the land at a price of £19,431, which was properly invested under the Settled Land Acts. Cohen, J., said he saw no reason why the exercise of the tenant for life's powers of sale should prevent the son's right of option to purchase from attaching to the proceeds of sale. Under Section 75 (5) of the Settled Land Act, 1925, the proceeds were to be treated as land, and there was authority for holding that the option to purchase was equally exercisable over the land or over the proceeds thereof.

Wills—Investment Clause—Power of Beneficiary to direct Investments.

In framing the investment clause of a will, it is common practice to enlarge the range of permitted investments, *e.g.*, so that trust funds may be invested in a family business. Thereby it is sometimes easier to provide a fair income for beneficiaries taking life interests. In *Re Hart's Will Trusts* (1943, 2 All E.R. 557), Bennett, J., had to decide whether a beneficiary may direct trustees to purchase shares from himself. By her will and codicil, the testatrix directed the sale and conversion of the residue of her real and personal estate, and provided that a sum of £2,000 and a share of residue should be held in trust for E.S.H. for life, the trustees to invest the capital of the trust fund in such investments as E.S.H. should from time to time direct, whether or not they were authorised investments. The trustees took out a summons to determine the extent of the power to direct the investments, and, in particular, whether, if E.S.H. so directed, they were to purchase shares from E.S.H. as vendor; and whether the power only applied to capital moneys in hand, or extended to

the realisation of sufficient investments then held, in order to provide the purchase money. Bennett, J., held: (1) on the true construction of the direction, the trustees were required, if practicable, to consult E.S.H. both as to investments and sales, and if he refused or failed to act, they were free to act themselves. (2) Provided he acted in good faith, E.S.H. might direct the purchase of shares from himself, and his power to direct was not confined to the investment of uninvested funds in the trustees' hands, but extended to the conversion of existing investments of the trust funds. The trustees must be satisfied that a reasonable and proper price was paid for the shares.

MISCELLANEOUS

Mortgage—Receiver—Duty to account to Mortgagee.

In *Leicester Permanent Building Society* v. *Butt* (1943, 2 All E.R. 523), Bennett, J., decided a question not governed by previous authority, namely, whether the receiver, who is the agent of a mortgagor, can be called to account by the mortgagee by whom he was appointed. It is provided by the Law of Property Act, 1925, Section 109 (2) that a receiver appointed under the powers conferred by that Act shall be deemed to be the agent of the mortgagor, and that the mortgagor shall be solely responsible for the receiver's acts or defaults unless the mortgage deed otherwise provides. In the present case there was no suggestion that the mortgage deeds did "otherwise provide." All four mortgages had been executed before September, 1939. After September, 1939, the plaintiffs, who were the mortgagees, wished to appoint a receiver of the rents and properties, and they duly obtained leave of the Court to appoint a receiver. In 1940 they appointed the defendant to be the receiver. Subsequently the plaintiffs requested the defendant to account for his receipts as receiver. On his refusal, the plaintiffs brought a summons before Cohen, J., claiming an account. It was argued that as the defendant was the agent of the mortgagor, he was not bound to account to the mortgagee. It was held by Bennett, J., however, that Section 109 of the Law of Property Act, 1925, imposes a statutory duty on a receiver, and that as the mortgagee is clearly interested in the performance of that duty, he is thereby entitled to an account.

The Emergency Acts and Orders

In our November, 1939, issue we published the first instalment of a comprehensive guide to the wartime enactments and Orders which most concern the accountant. The forty-sixth instalment is given below. The summaries are not intended to be exhaustive, but only to give the main content of an Act or Order, the full text of which should be consulted if details are required.

ACTS

Income Tax (Employments) Act, 1943

Income tax for 1944-45 and subsequent years on the pay of manual workers, and of other employees if their remuneration is calculated by reference to any period less than a month or does not exceed £600 per annum, and on pensions up to £600, is to be assessed on the amount of the emoluments for the year. Deductions and repayments are to be made under Inland Revenue regulations.

(See pages 43 and 52 of this issue.)

Price Control (Regulation of Disposal of Stocks) Act, 1943

The Board of Trade may issue licences permitting traders to restrict sales of price-controlled goods to particular classes of buyers.

ORDERS

FINANCE

No. 1436. *Clearing Office (Italy) Amendment Order*, 1943

The Clearing Office (Italy) Order, 1936, is not applicable to payments for Italian goods imported into the United Kingdom after October 8, 1943.

No. 1472. *Blocked Accounts (Authorised Investments) Order*, 1943

A revised list is given of Government securities in which sums standing to the credit of a blocked account may be invested.

No. 1484. *Securities (Exemption) (Amendment) Order*, 1943

Certain Mexican Government securities are no longer exempted from the provisions of Regulation 1 of the Defence (Finance) Regulations.

(See ACCOUNTANCY, November, 1943, page 39.)

PRICES OF GOODS AND SERVICES

No. 1338. *Enamelled Hollow-ware (Maximum Prices) Order*, 1943.

No. 1339. *Hollow-ware and Kitchen Hardware (Control of Manufacture and Supply) (No. 3) Order*, 1943.

No. 1338 fixes maximum wholesale and retail prices for vitreous enamelled wrought steel hollow-ware and tinplate lids. No. 1339 fixes maximum prices for manufacturers, and also contains provisions relating to marking of goods and invoices.

(See ACCOUNTANCY, November, 1943, page 39.)

PUBLIC UTILITIES

No. 1326. *Regulations with respect to the Accounts of the Port of London Authority*

Shillings and pence may be omitted, and a few other amendments are made in the form in which the Port of London Authority accounts are to be drawn up.

TRADING WITH THE ENEMY

No. 1417. *Trading with the Enemy (Custodian) (China) Order*, 1943

Money payable by a banker to a person in any area of China (excluding Manchuria) in enemy occupation need not be paid to the Custodian unless so directed by the Board of Trade.

No. 1491. *Trading with the Enemy (Specified Persons) (Amendment) (No. 15) Order*, 1943

Further amendments are made in the list of persons with whom dealings are prohibited.

(See ACCOUNTANCY, November, 1943, page 39.)

WAR RISKS INSURANCE

No. 1578. *War Risks (Commodity Insurance) (No. 4) Order*, 1943

Premiums under the commodity insurance scheme for the three months commencing December 3, 1943, are to be at the rate of 5s. per cent.

(See ACCOUNTANCY, September, 1943, page 242.)

Society of Incorporated Accountants

COUNCIL MEETING

WEDNESDAY, OCTOBER 27, 1943

Present: Mr. Richard A. Witty (President) in the Chair, Mr. Fred Woolley (Vice-President), Mr. F. J. Alban, Mr. A. Stuart Allen, Mr. R. Wilson Bartlett, Mr. Robert Bell, Mr. R. M. Branson, Mr. J. Paterson Brodie, Mr. W. Norman Bubb, Mr. W. Allison Davies, Mr. E. Cassleton Elliott, Mr. M. J. Faulks, Mr. C. A. G. Hewson, Mr. Walter Holman, Mr. Bertram Nelson, Mr. James Paterson, Mr. F. A. Prior, Mr. R. E. Starkie, Mr. Joseph Stephenson, Mr. Percy Toothill, Mr. Joseph Turner, and Mr. A. A. Garrett (Secretary).

New Zealand Society of Accountants

It was reported that Dr. A. J. Harrop, the representative in London of the University of New Zealand, had requested that facilities be granted to certain candidates serving in the Royal New Zealand Forces who wished to qualify for membership of the New Zealand Society of Accountants. The Council confirmed the decision of the Examination and Membership Committee that candidates nominated by the University of New Zealand be allowed to present themselves for certain papers at the Society's examinations held in Great Britain.

Post-War Problems Affecting Members and Candidates

It was reported that the Examination and Membership Committee had appointed a sub-committee to consider problems arising from the return from H.M. Forces of members and candidates. The sub-committee was asked to present a report on the widest basis.

Sir James Martin Memorial Exhibition

The Council adopted the recommendation of the appropriate Committee that the Sir James Martin Memorial Exhibition in respect of the July, 1943, Intermediate Examination be awarded to Mr. Frank Holloway, Articled Clerk to Mr. Frank Hall, F.S.A.A., Leeds.

Resignations

The resignations of the following members were accepted with regret:—

From December 31, 1943:

Cox, T. (Associate), London.
Higgs, A (Associate), Potters Bar.
Mason, F. G. (Associate), Barnsley.

From January 31, 1944:

Dodd, H. (Associate), London.

Deaths

The Secretary reported the death of each of the following members:

Ball, H. (Associate), Bedford.
Bates, A. (Fellow), Stoke on Trent.
Brown, T. Booth (Fellow), Manchester.
Colton, T. (Associate), Manchester.
Cox, S. W. (Associate), Cape Town.
Heatley, N. K. (Fellow), Manchester.
Jackson, G. W. (Associate), Sao Paulo, Brazil (through enemy action).
Magennis, A. J. (Fellow), Cork.
Martin, J. W. (Associate), London.
Read, H. A. (Fellow), Johannesburg.
Spencer, G. W. (Fellow), London.
Titterton, J. P. (Associate), Southend-on-Sea.

RESULTS OF EXAMINATIONS IN INDIA

DECEMBER, 1942

The Examination and Membership Committee have declared that the following candidates passed the Society's Intermediate Examination. Special arrangements were made for the examinations to be held in Delhi in December, 1942, for the convenience of candidates serving articles of clerkship in India, who were unable to proceed to Great Britain for the examinations.

Passed in Intermediate

Alphabetical Order

Alies, Michael John, B.Sc., Clerk to R. A. Patel & Co., Colombo.
Chanduwadia, Jehanbux Shavaksha, B.Com., Clerk to S. B. Billimoria, Bombay.
Cooper, Russi Naveroji, Clerk to K. S. Engineer (Sorab S. Engineer & Co.), Bombay.
Kapadia, Karasandas Mulji, B.Com., Clerk to N. M. Raiji (N. M. Raiji & Co.), Bombay.
Kapadia, Promode Lalbhai, B.Com., Clerk to Batliboi & Purohit, Bombay.
Mama, Sorab Gustasp, Clerk to Sorab S. Engineer, (Sorab S. Engineer & Co.), Bombay.
Marwary, Basudeo, B.Com., Clerk to K. N. Gutgutia, Calcutta.
Mehra, Guru Datta, formerly Clerk to K. P. Soni & Co., Lahore.
Mehta, Ramniklal Madhavji, Clerk to N. M. Raiji (N. M. Raiji & Co.), Bombay.
Saha, Girindra Mohan, Clerk to G. Basu & Co., Calcutta.
Sastri, Dorbalala Balagangahara, formerly Clerk to Sastri & Shah, Madras.
Shah, Dhansukhlal Kalidas, Clerk to N. J. Shah (Dalal & Shah), Bombay.
Sen, Parbati Sankar, Clerk to J. Sen & Co., Calcutta.
Tadvalkar, Madhav Keshav, B.Sc., Clerk to R. P. Dalal (Dalal, Desai & Co.), Bombay.

Summary:—

14 *Candidates Passed.*
38 *Candidates Failed.*

52 Total.

Three candidates failed in the Final Examination.

SCOTTISH BRANCH

A meeting of the Scottish Council was held in Glasgow, on Friday, November 5. Mr. Robert T. Dunlop, President of the Scottish Branch, was in the chair and there was a good attendance. The Secretary, Mr. James Paterson, reported on a number of matters of interest to the profession in Scotland. A number of applications for exemption from the Preliminary Examination and for permission to sit the examinations were reported and appropriately dealt with.

PERSONAL NOTES

Mr. F. Dall Gray, Incorporated Accountant, of the firm of Lawther, Bass & Gray, Incorporated Accountants, Coleraine, has taken into partnership Mr. J. S. Patterson, Chartered and Incorporated Accountant, and Mr. F. G. Stokes Dunbar, Incorporated Accountant, both of whom have been associated with the firm for several years. The name of the firm remains unchanged.

Messrs. Duck, Mansfield & Co., Incorporated Accountants, 66, Broad Street Avenue, London, E.C.2, announce that they have taken into partnership Mr. D. G. Light, Incorporated Accountant, who has been associated with them for the past 20 years. The name of the firm remains unchanged.

Messrs. Cassleton Elliott & Co., 4 and 6, Throgmorton Avenue, London, have admitted Mr. G. C. Baker, Incorporated Accountant, into partnership in respect of their branch in Jos (Nigeria).

Mr. Alfred Wright intimates that, owing to the much-regretted death of his partner, Mr. Edward A. Wright, he has taken into partnership Mr. Douglas H. Aris, who has been with the firm for nearly 25 years. The practice will continue to be carried on under the style of Alfred Wright and Co., Incorporated Accountants, at 9-10, Fell Road, Croydon, Surrey, with London consulting rooms at 6, Duke Street, St. James's, S.W.1.